

STATE OF HAWAII
DEPARTMENT OF LAND AND NATURAL RESOURCES
Land Division
Honolulu, Hawaii 96813

September 14, 2018

Board of Land and Natural Resources
State of Hawaii
Honolulu, Hawaii

PSF No.: 18OD-078

Oahu

Sale of Lease and Conveyance of Leasehold Commercial Improvements
by Bill of Sale at Public Auction for Business, Commercial or
Industrial Purposes, Waipahu, Ewa, Oahu, Tax Map Key: (1) 9-4-
049:062.

LEGAL REFERENCES:

Sections 171-14, -16, -17, -36 and other applicable sections of
Chapter 171, Hawaii Revised Statutes (HRS), as amended.

LOCATION:

Portion of Government lands situated at Waipahu Industrial Park,
Ho'ae'ae, Ewa, Oahu, identified by Tax Map Key: (1) 9-4-049:062,
as shown on the attached maps labeled Exhibit 1A, 1B & 1C.

AREA:

18,410 square feet of land and a two-story commercial structure
consisting of 12,800 square feet, more or less.

ZONING:

State Land Use District: Urban
City & County of Honolulu CZO: I-2

TRUST LAND STATUS:

Section 5(a) lands of the Hawaii Admission Act

DHHL 30% entitlement lands pursuant to the Hawaii State
Constitution: YES _____ NO X

CURRENT USE STATUS:

See attached Exhibit 3 for current use status.

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CHARACTER OF USE:

Business, industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance.

LEASE TERM:

Sixty-five (65) years from the commencement date of the lease.

COMMENCEMENT DATE:

Sixty (60) days after the date of sale; provided that if such date is not on the first day of any month, the commencement date shall be the first day of the month following such date; and further provided that the Chairperson may amend the commencement date for good cause.

MINIMUM UPSET ANNUAL RENT AND CONVEYANCE OF LEASEHOLD IMPROVEMENTS:

To be determined by independent appraisal establishing fair market rent, subject to review and approval by the Chairperson. The appraisal shall determine the upset rent for the land for the first ten years of the lease, as well as an appropriate stepped increase (as a percentage increase over the base rent of the immediately preceding 10-year period) for the second and third 10-year periods to provide the successful bidder with a known rent for the first 30 years of the lease. The appraiser procured to determine the upset rent shall also separately determine the fair market value of the existing improvements on the land.

METHOD OF PAYMENT:

Semi-annual payments, in advance.

RENTAL REOPENINGS:

At the end of the 30th, 40th, 50 and 60th years of the lease term, by staff or independent appraisal.

PERFORMANCE BOND:

Twice the annual rental amount.

MINIMUM IMPROVEMENTS:

Within one year from the commencement date of the lease, the Lessee shall have completed the deferred maintenance items listed on Exhibit 4 having a value of not less than \$126,000.00. Said maintenance items shall be in accordance with plans submitted to

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the Chairperson for approval prior to their construction.

CONSTRUCTION BOND:

Amount of deferred maintenance.

RENT WAIVER:

The rent may be waived for a maximum period of twelve (12) calendar months upon substantial completion of the deferred maintenance items listed on Exhibit 4. "Substantial completion" for purposes of the lease will mean a value equal to at least 90% of the estimated deferred maintenance expense.

PROPERTY CHARACTERISTICS:

Utilities - Water, sewer, electricity and telephone

Existing Improvements - Two-story concrete masonry unit commercial structure with a rentable area of approximately 12,800 square feet.

Legal access to property - Staff has verified that there is legal access to the property off of Leokane Street.

Subdivision - Staff has verified that the subject property to be auctioned is a legally subdivided lot.

Encumbrances - Staff has verified that the following encumbrances exist on the property: See attached Exhibit 3 for list of encumbrances.

CHAPTER 343 - ENVIRONMENTAL ASSESSMENT:

In accordance with the "Exemption List for the Department of Land and Natural Resources", approved by the Environmental Council and dated June 5, 2015, the subject request is exempt from the preparation of an environmental assessment pursuant to Exemption Class No. 1, Item No. 47, (See Exhibit 2) that states "Leases of State land involving negligible or no expansion or change of use beyond that previously existing." Once the lease is acquired, should the successful bidder desire to change the use materially from the existing use, the successful bidder will be responsible for compliance with Chapter 343, HRS, with respect to any increased development or change in use of the property from the existing use.

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REMARKS:

The subject parcel consists of approximately 18,410 square feet of land together with a two-story concrete masonry unit commercial structure with nine individual units and a gross leasable area of approximately 12,800 square feet. The Department acquired this property through an Exchange Deed dated February 21, 2014 between the State of Hawaii and Hawaii Baptist Academy for the purpose of increasing public land trust revenue in order to support the public land trust and the Department's fiduciary duties. The building was 100% occupied at the time of acquisition. At its meeting on December 13, 2013, under agenda item D-32, the Board granted its final approval of the exchange and authorized the issuance of revocable permits for the property's existing tenants. With the exception of one holdover tenant, staff has accomplished this.

Staff contracted with Colliers International (Colliers) for a *Lease and Sale Analysis* report to evaluate which of the following two actions would be most advantageous to the State: the sale at public auction of leasehold improvements in conjunction with a new ground lease (Option 1)¹; or the sale at public auction of a lease for land and improvements (Option 2)². In addition, staff asked Colliers to recommend the lease term that would be most desirable for potential bidders at public auction. Colliers' evaluation concluded that Option 1, with a lease term of 65 years, would be most attractive to potential investors and produce the highest revenue for the State. Colliers also calculated the present value of the cash flow keeping these revocable permits in place for the same period of time (see table below).

1 Colliers determined the price for the leasehold improvements by discounting the cash flow an investor would realize over the term of the lease (i.e. gross rent less operating expenses, real property taxes and lease rent less capital expenses/reserves). They also assumed the proceeds from the sale of the improvements would be reinvested and provide a return of 3% (based on the 30-year T-Bill rate). Colliers used two scenarios, sales comparable approach and the assessed land value approach, to value the ground lease, and a 7% return for each scenario, fixed for 10-years.

2 To evaluate this option, Colliers assumed two types of bidders: investors and owner users. They assumed an investor would pay an annual master lease rent of \$113,664, which would allow for an 8% annual return. They also assumed a capital improvement reserve for the entire lease term. Colliers assumed an owner user would pay an annual master lease rent of \$158,208. They assumed no capital improvement reserves for the entire lease term.

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SUMMARY OF FINDINGS			
Scenario	Revenue to DLNR Present Value		
	Sale of Improvements	Lease Rents	Total
OPTION 1: LEASEHOLD SALE & GROUND LEASE (1)			
Ground lease based on market land value	\$617,791	\$2,054,616	\$2,672,406
Ground lease based on assessed land value	\$894,943	\$1,457,882	\$2,352,825
OPTION 2: MASTER LEASE			
20-year Master Lease Cash Flow (Investor)	n/a	\$1,328,039	\$1,328,039
20-year Master Lease Cash Flow (User)	n/a	\$1,586,618	\$1,586,618
65-years of Master Lease Cash Flow (Investor)	n/a	\$2,288,995	\$2,288,995
65-years of Master Lease Cash Flow (User)	n/a	\$2,465,219	\$2,465,219
STATUS QUO. DLNR HOLD			
65-year Cash Flow using Existing Rents	n/a	\$2,210,078	\$2,210,078
65-year Cash Flow using Market Rents	n/a	\$3,087,790	\$3,087,790

(1) Does not include projected reinvestment returns from sale of leasehold improvements.

Staff is therefore recommending that the Board authorize the auction of a new 65-year lease covering the land of the subject parcel, and the sale of the leasehold improvements to the successful bidder. As mentioned above, the subject property consists of an approximately 18,410 square foot lot and an approximately 12,800 square foot structure.

Staff anticipates that the successful bidder (lessee) will issue sub-space leases for the individual units within the building. Staff believes that due to the competitive nature of the Oahu commercial real estate market, the lessee will need to act expeditiously to sublet the premises to avoid vacancies and maintain a healthy cash flow. However, the Department's standard sublease language, as required under Hawaii Revised Statutes Section 171-36(a)(6), provides:

The Lessee shall not rent or sublet the whole or any portion of the premises, without the prior written approval of the Board; provided, however, that prior to this approval, the Board shall have the right to review and approve the rent to be charged to the proposed sublessee and that in the case where the Lessee is required to pay rent based on a percentage of its gross receipts, the receipts of the sublessee or any subsequent sublessee shall be included as part of the Lessee's gross receipts, and the Board shall have the right to revise the rent for the premises based upon the rental rate charged to the sublessee including the percentage rent, if applicable, and proved, further, that the rent may not be revised downward. For good cause, the Board may waive the requirement that the Lessee obtain prior written approval to rent or sublet

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all or any portion of the premises.

Staff therefore recommends that the auction lease contain a provision allowing the lessee to sublet without Board consent pursuant to HRS Section 171-36 (b), which provides in relevant part:

"(b) The board, from time to time, upon the issuance or during the term of any intensive agricultural, aquaculture, commercial, mariculture, special livestock, pasture, or industrial lease, may:

(1) Modify or eliminate any of the restrictions specified in subsection (a);. . .

to the extent necessary to qualify the lease for mortgage lending or guaranty purposes with any federal mortgage lending agency, to qualify the lessee for any state or private lending institution loan, private loan guaranteed by the State, or any loan in which the State and any private lender participates, or to amortize the cost of substantial improvements to the demised premises that are paid for by the lessee without institutional financing"

Furthermore, with respect to the lessee subletting the premises without the Board's approval, Act 103 Session Laws of Hawaii 2002 (Act 103) states, *"The board may waive the requirement to obtain approval for good cause"*³

Given the unique nature of this property within the Division's portfolio (i.e. a multi-tenant commercial property), the expenditure of not less than \$126,000 required to address the deferred maintenance issues at the property, which will either be self-financed or financed through a mortgage, and the timeliness with which the lessee will need to act to keep the property fully occupied, staff recommends that the Board use its discretion, as allowed under HRS 171-36(b) and Act 103, to include a provision in the auction lease allowing the lessee to sublet without Board consent. In addition, staff recommends the sub-space leases be freely assignable without the Board's consent, and without any premium being owed to the Board.

The Board has previously stated its desire to convert revocable permits to long term dispositions, where possible. At present, no statutory mechanism exists to allow staff to issue space leases

³ For reasons staff is unable to determine, Act 103 has not been codified into the official version of the Hawaii Revised Statutes.

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for the individual permittees at the subject property. Staff believes the sale of a lease at public auction is the means to achieve this objective.

Staff solicited comments from the Office of Hawaiian Affairs, Board of Water Supply, the City and County of Honolulu's Departments of Planning, Parks & Recreation and Facility Management. The Board of Water Supply had no objections and concurred with the exemption notification. The Department of Planning and Permitting's comments are attached as Exhibit 5. The successful bidder will be required to comply with any SMA requirements applicable to any increased development or change in use as referenced in Exhibit 5. None of the other agencies replied by the suspense date.

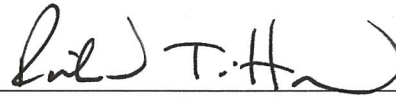
RECOMMENDATION: That the Board:

1. Declare that, after considering the potential effects of the proposed disposition as provided by Chapter 343, HRS, and Chapter 11-200, Hawaii Administrative Rules, this project will probably have minimal or no significant effect on the environment and is therefore exempt from the preparation of an environmental assessment.
2. Authorize the sale of a lease and conveyance of leasehold commercial improvements by bill of sale at public auction covering the subject area for business, commercial or industrial purposes under the terms and conditions cited above, which are by this reference incorporated herein and further subject to the following:
 - a. The standard terms and conditions of the most current business, commercial or industrial general lease form, as may be amended from time to time, to include any special terms or conditions regarding subleasing that the Department of the Attorney General deems advisable including, but not limited to, term, character of use, compliance with laws, compliance with ground lease, indemnity, insurance and termination;
 - b. The rent may be waived for a maximum of twelve (12) calendar months upon substantial completion of the deferred maintenance items contained in Exhibit 4;
 - c. Review and approval by the Department of the Attorney General; and

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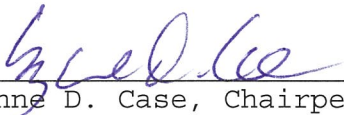
- d. Such other terms and conditions as may be prescribed by the Chairperson to best serve the interests of the State.
3. The Board find there is good cause to waive the sublease approval requirement under HRS Section 171-36(a)(6) pursuant to Act 103 SLH 2002, to the extent the Department of the Attorney General determines Act 103 is good law.

Respectfully Submitted,



Richard T. Howard

APPROVED FOR SUBMITTAL:



Suzanne D. Case, Chairperson

March 21, 1997 Vol. 31, No. 3

POR. "WAIPAHU INDUSTRIAL PARK," FILE PLAN 973, L. C. AM. 10474:9, HOAEAE, EWA, OAHU. (Formerly por. 9-4-01.)

FOR REAL PROPERTY TAXATION PURPOSES
SUBJECT TO CHANGE



EXHIBIT "1B"



EXHIBIT "1c"

EXEMPTION NOTIFICATION

Regarding the preparation of an environmental assessment pursuant to Chapter 343, HRS and Chapter 11-200, HAR

Project Title:	Sale of Master Lease at Public Auction for Business, Commercial or Industrial Purposes.
Project / Reference No.:	PSF No. 18OD-078
Project Location:	Waipahu Industrial Park, Ho'ae'ae, Ewa, Oahu, identified by Tax Map Key: (1) 9-4-049:062
Project Description:	Sale of Master Lease at Public Auction for Business, Commercial or Industrial Purposes.
Chap. 343 Trigger(s):	Use of State Land
Exemption Class No.:	<p>In accordance with Hawaii Administrative Rule Section 11-200-8 and the Exemption List for the Department of Land and Natural Resources reviewed and concurred by the Environmental Council on June 5, 2015, the subject request is exempt from the preparation of an environmental assessment pursuant to Exemption Class No. 1, "Operations, repairs or maintenance of existing structures, facilities, equipment, or topographical features, involving negligible or no expansion or change of use beyond that previously existing," Item 47, which states the "Leases of state land involving negligible or no expansion or change of use beyond that previously existing."</p> <p>As the proposed action involves the sale of the master lease at public auction, the tenant will be responsible for compliance with Chapter 343, HRS, in the event it proposes any development of the land that is not exempt from Chapter 343. As such, staff believes that the sale of the lease at public auction involves negligible or no expansion or change of use beyond that previously existing, and should therefore be found exempt from the preparation of an environmental assessment under Chapter 343, HRS.</p>
Cumulative Impact of Planned Successive Actions in Same Place Significant?	No, the requested location has been used for business/industrial purposed since its construction in 1975. Therefore, staff believes the sale of the master lease at public auction has no significant effect on the environment.

EXHIBIT 2

Action May Have
Significant Impact on
Particularly Sensitive
Environment?

No.

Analysis:

The request pertains to selling a master lease for the subject location. Other lots in the area have been used for similar purposes for decades. Staff believes that the request would involve negligible or no expansion or change in use of the subject location beyond that previously existing.

Consulted Parties

Agencies listed in submittal.

Recommendation:

It is recommended that the Board find this project will probably have minimal or no significant effect on the environment and is presumed to be exempt from the preparation of an environmental assessment.

EXHIBIT 2

Doc. No.	Permittee Name	Permitted Use	Area	Gross Monthly Rent
rp7853	Ernest Lum	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	2,725 s.f.	\$2,433.97
rp7854	Gary Lucero	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	1,222 s.f.	\$1,079.09
rp7856	Kai Construction Hawaii, Inc.	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	1,350 s.f.	\$1,205.82
rp7857	John Wisniewski	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	1,375 s.f.	\$1,224.09
rp7858	Tachibana Painting LLC	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	1,350 s.f.	\$1,315.44
rp7859	John Wisniewski	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	728 s.f.	\$654.66
rp7860	Vidal Alfonso	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	1,350 s.f.	\$1,205.82
rp7861	Warhorse Strength Camp LLC	Industrial and/or commercial uses permitted under the City and County of Honolulu Land Use Ordinance	1,350 s.f.	\$1,205.82
Holdover	Jonathan Kamaka	Apparel Printing Services	1,350 s.f.	\$1,109.90

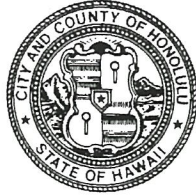
94-143 Leokane St. Deferred Maintenance

Item	Estimated Cost
Paint exterior walls	\$30,000
Install safety nosing on stairs	\$ 3,000
Repair and clean hard rails and pickets	\$ 1,000
Install fluid coating on lanais	\$ 4,500
Install fluid coating on deck and ramp	\$10,000
Replace gutters and downspouts	\$ 6,300
Replace aging and deteriorating sanitary lines	\$10,000
Install backflow prevention device	\$10,000
Repair concrete parking slab	\$35,000
Patch roof check slope to eliminate ponding	\$16,500
Total	\$126,300

DEPARTMENT OF PLANNING AND PERMITTING
CITY AND COUNTY OF HONOLULU

650 SOUTH KING STREET, 7TH FLOOR • HONOLULU, HAWAII 96813
PHONE: (808) 768-8000 • FAX: (808) 768-6041
DEPT. WEB SITE: www.honolulu.dpp.org • CITY WEB SITE: www.honolulu.gov

KIRK CALDWELL
MAYOR



KATHY K. SOKUGAWA
ACTING DIRECTOR

TIMOTHY F. T. HIU
DEPUTY DIRECTOR

EUGENE H. TAKAHASHI
DEPUTY DIRECTOR

2018/ELOG-1230 (at)

July 18, 2018

Mr. Richard T. Howard
Land Agent
Department of Land and Natural Resources
Land Division
State of Hawaii
P.O. Box 621
Honolulu, Hawaii 96809

RECEIVED
LAND DIVISION
2018 JUL 20 AM 11:08
DEPT OF LAND &
NATURAL RESOURCES
STATE OF HAWAII

Dear Mr. Howard:

SUBJECT: Request for Comments on Sale of Master Lease at Public Auction for Business, Commercial, or Industrial Purposes, Waipahu, Ewa, Oahu, Tax Map Key: (1) 9-4-049: 062

We received your letter on June 18, 2018, requesting comments on the Sale of Master Lease, as referenced above. We offer the following comments and recommendations.

1. The subject property is in the Special Management Area (SMA). Any proposal that is considered "development" pursuant to Section 25-1.3, Revised Ordinances of Honolulu, will require an SMA Permit. Any development that is valued at more than \$500,000 will require an SMA Use Permit.
2. The subject property is also located within the Transit-Oriented Development (TOD) Special District, and additional design standards apply to redevelopment projects.
3. The Waipahu Neighborhood TOD Plan highlights the need to create and improve connectivity and circulation through the rail station areas. If this site is to be redeveloped in the future, the TOD Plan recognizes the opportunity for creating public access between the Leeward Bikeway and Leokane Street at or near this site (the Leeward Bikeway is also referred to as the Pearl Harbor Historic Trail in the TOD Plan.) The State Department of Transportation has an ongoing improvement project along the Leeward Bikeway.

EXHIBIT "5"

Mr. Richard T. Howard
July 18, 2018
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4. While the TOD Plan proposed a recreational park in this location, the current zoning of the property is Industrial-Intensive. The vision outlined in the TOD Plan should be considered again in the future, at the end of the Master Lease's terms.

Thank you for the opportunity to provide input for the sale. Should you have any questions, please contact Andrew Tang of our staff, at 768-8123 or andrew.tang@honolulu.gov.

Very truly yours,

A handwritten signature in dark ink, appearing to read "Kathy K. Sokugawa". The signature is fluid and cursive, with the first name "Kathy" being more prominent.

Kathy K. Sokugawa
Acting Director